C-31

Via Email to lgprogram@hq.doe.gov

SUBJECT: RIN 1901-AB21 – Loan Guarantees for Projects that Employ Innovative Technologies: Notice of Proposed Rulemaking (NOPR) and Opportunity for Comment

Excelsior Energy Inc. ("Excelsior"), appreciates the opportunity to comment on the subject Notice of Proposed Rulemaking ("NOPR"). Excelsior is the project developer for the Mesaba Energy Project, an Integrated Gasification Combined Cycle ("IGCC") electric power generating station to be fueled by subbituminous coal, bituminous coal, and petroleum coke, with nameplate capacity of 740 Megawatts and nominally rated to deliver approximately 600 MW (net) of electricity.

The Mesaba Energy Project represents one of the most advanced IGCC projects in the country. It will be the first multi-train IGCC facility and will be implemented with a commercial structure to provide power at a competitive price. It will demonstrate that IGCC is a commercially viable power generation option, thereby directly addressing the primary remaining obstacle to widespread market penetration of this critical element of the nation's energy and environmental strategy.

Excelsior's mission is to bring new power generation capacity, economic development, and reduced levels of pollution to Minnesota through the use of an innovative and advanced energy technology. Excelsior believes that IGCC technology is a critical component of comprehensive national energy security and environmental protection strategies and that the Project furthers these national priorities.

Comments to the Introduction and Background

The Energy Policy Act of 2005 authorizes loan guarantees for "advanced fossil energy technology" as the NOPR recognizes (at 5), but the NOPR then calls out "carbon sequestration optimized coal power plants" (at 7)—a phrase not used or defined in the statute or anywhere else in the proposed rule. The Department of Energy ("DOE") should clarify that this undefined phrase is illustrative only, and not limiting.

DOE argues that "nothing" in Title XVII requires that all solicitations implementing the program be open to every project "arguably eligible" and that DOE therefore has discretion to "tailor" solicitations to meet "programmatic objectives." While this is true as a general rule, DOE's discretion is limited by the fact that Congress specifically authorized loan guarantees for certain projects listed in Section 1703(c), including the Mesaba Energy Project. DOE should structure the program to ensure that those specifically authorized projects receive loan guarantees before it tailors solicitations to meet other, non-statutory programmatic objectives.

DOE recognizes (at 7), that Public Law 110-5 provides $4 billion in statutory loan guarantee authority, but does not explicitly state that DOE will apply this $4 billion to the Section 1703(c) projects who submitted Pre-Applications under DOE's first solicitation. It is clear that Congress first authorized specific projects for loan guarantees in EPAct 2005, and then provided the requisite appropriations authorization for those projects in Public Law 110-5. DOE should clarify that it intends to apply the $4 billion to those projects with specific statutory authorization. Statutorily-authorized projects like Mesaba who submitted pre-applications pursuant to the August 2006 solicitation did so in order to provide DOE the information it needs to issue the authorized loan guarantee; they are not competing with unauthorized projects who similarly submitted pre-applications.

We support DOE's position that provisions of the rule can apply to projects for which Pre-Applications were submitted under the first solicitation if both DOE and the Applicant agree. We support DOE's position that absent such an agreement, any conflicts between the guidance issued with the first solicitation and this rule will be resolved by adherence to the terms of the guidance.

We support DOE's position that projects that are solely research, development or demonstration projects will not be eligible for loan guarantees. The purpose of the loan guarantee program is to foster the commercial deployment of new technologies; other sources of funding are available to advance important RD&D activities.

Comments to proposed section 609.2

DOE specifically requested comments on the two alternatives for construing the phrase "in general use" in the definition of commercial technology, essentially offering a choice between five projects "ordered for, installed in, or used in" the United States versus one project that has been in operation for five years. It is difficult to see the justification for such a restrictive definition of the phrase "in general use." The financial community has displayed great reticence to provide debt at reasonable commercial interest rates in support of new technologies that have not been widely demonstrated to operate successfully over a sustained time period. The mere placement of orders for new technologies does not address in any way the financial community's perception of unacceptable technology operational risk. Therefore, it is unlikely that the cost of capital will be at all comparable to conventional energy technologies for new technologies that have simply been ordered five times, or after the successful commercial operation of only one project for a period of only five years. Five orders for a particular technology, without successful commercial demonstration over a period of time, will not be sufficient for the bank market to accept the technology as commercial and credit-worthy.

More importantly, a loan guarantee that is issued but never exercised represents relatively insignificant costs to the U.S. government. Indeed, if the applicant provides both a non-refundable credit subsidy and administrative fees that cover the government's costs, projects that repay their debt obligations without triggering the government guarantee represent revenue raisers for the government. Thus, there is a strong public policy argument to make that DOE should err on the side of providing too many loan guarantees, rather than too few.

Once a technology is truly in "general use"—as defined by the marketplace—then government loan guarantees will no longer be necessary for the project developers. Further, given the great differences between technology systems covered by the loan guarantee program, technology components that differ within those systems, and the markets in which those technology systems are deployed, it is unlikely that a single definition based on a bright line number of projects or years of operation will be more efficient than relying on market forces to determine when a project can be efficiently financed without government loan guarantees.

If DOE believes it must adopt a bright line test, however, then for IGCC systems, the best policy is to combine the two alternatives offered by DOE into one modified definition. Thus, a particular technology component deployed in an IGCC project would be considered to be in general use if it has been operational in five or more projects in the United States for a period of five years.

We support DOE's position that attributes that will be considered in determining whether a technology is "new or significantly improved" must relate to energy production, use, efficiency, or transportation, rather than tangential qualities like aesthetics. DOE's definition of the phrase "new or significantly improved"—either "recently discovered or learned" or that "involve or constitute meaningful and important improvements in the productivity or the value of the technology" appears to be workable, but must be read in concert with DOE's definition of "commercial technologies" as discussed above.

<u>Comments to Section 609.4</u>

While Excelsior has submitted a Pre-Application in response to the August 2006 solicitation and is fully capable of meeting the requirements of that solicitation, the requirements for the content of the Pre-Application result in unnecessary expenditures of time and effort on both the part of an applicant and on the part of the DOE review teams. There are elements of the requirements, such as a "copy of a commitment letter from an Eligible Lender or other Holder expressing its commitment to provide the required debt financing necessary to fully construct and fully commission the project," and a "copy of the equity commitment letter(s) from each of the Project Sponsors" that are difficult, if not impossible, to provide at such an early stage of discussion about a potential federal loan guarantee. Excelsior suggests that DOE review the required content of the Pre-Application and move items that are more appropriate for later stages of negotiations to the Application phase. Even there, it is important for DOE to recognize that project financing among multiple parties is an iterative process and that final commitments from any one party depend entirely on final commitments from all. A number of the proposed Application requirements set forth in the NOPR (such as numbers 8, 9, 10, 12, 14, 18, 19, 23, 24 and 26) are overly detailed or more properly characterized as "conditions to closing" that are more in the nature of confirmatory diligence items than requirements DOE must have to make its initial evaluation and decision about a particular application. DOE should recognize that the negotiation process contains many more steps than a pre-application and an application phase, and that it is customary practice in the financial community to make continued progress in negotiations conditional on the production of documents and the securing of commitments that develop during the course of the negotiations themselves. Agreements can be reached that remain conditional on other items that simply cannot be secured until immediately prior to financial close. It is those "conditions to closing" that DOE should not require as part of the pre-application and application. Not only are many of these requirements inappropriate, or indeed simply unavailable at the time those documents are prepared, they are not in fact required in order for the DOE and other agencies to apply criteria and make the decisions contemplated at the time of the application phase.

Comments to Section 609.7

DOE includes in its evaluation factors at proposed Section 609.7(b)(9) the issue of whether and "to what extent the Applicant will rely upon other Federal and non-Federal government assistance such as grants, tax credits, or other loan guarantees to support" the project. It is appropriate for such a factor to be considered, and Excelsior supports the concept of significant private equity involvement in projects seeking loan guarantees. However, DOE's apparent bias against projects that are receiving other forms of government assistance is contrary to the statutory provisions in Title XVII at Section 1703(e) that provides that a "project that receives tax credits for clean coal technology shall not be disqualified from receiving a guarantee under this title."

For projects that do not qualify for a clean coal technology tax credit, it is appropriate that DOE includes reliance on other government assistance as an evaluation factor only, and not as one of the six disqualifying conditions listed at 609.7(a). There are several reasons for this policy choice. First, additional government assistance (such as in the case of the Mesaba Energy Project, a Clean Coal Power Initiative award from DOE) reduces total project costs that must be capitalized by the applicant, thus reducing the size of the loan guarantee, increasing the likelihood of debt repayment, and allowing DOE to better leverage its participation in a variety of projects. Second, the fact that a project has been successful in securing government assistance is a strong indicator of the project's strength, given the rigorous evaluation of projects that DOE conducts before providing assistance. That prior evaluation can then be employed as a "pre-screen" that identifies worthy projects for the subsequent loan guarantee, i.e., those projects that are most likely to result in debt repayment. Third, the fact that non-Federal governments, whether States or localities, are providing assistance to a project (as they have been for the Mesaba Energy Project) is a sign of strong political and community support for the project, which in turn is an indicator of project strength and a high likelihood of debt repayment.

As discussed above, when DOE issues a loan guarantee to a strong project that never triggers execution of the guarantee, the government actually receives a return on a quite modest investment. Thus, DOE would be better served by reversing the negative presumption set out in the "Discussion of Proposed Rule" section of the NOPR, and instead view the presence of other forms of Federal and non-Federal government assistance as a **positive** factor in evaluating loan guarantees applications.

Comments to Section 609.10

Excelsior understands that DOE has and will receive a great number of inquiries and comments about the issue of limiting the coverage of the loan guarantee to less than 100 percent of the total face value of the loan(s) or other debt obligation(s) (Section 609.10(d)((3)). It is clear that to the extent that there is full coverage of debt by a federal loan guarantee, capital costs will be lower than they would be under any partial coverage, and in some ways such partial coverage is a less efficient means of ensuring private sector participation than would be a simple requirement that equity participation be robust.

Compounding the inefficiency of the partial coverage approach in the NOPR is the provision, upon which DOE asked for specific comment, that prevents separating ("stripping") the guaranteed debt from the unguaranteed debt for purposes of marketing it in the secondary debt market (Section 609.10(d)(4)). Excelsior understands that the financial markets are ill-equipped to handle the hybrid instruments that would result from this policy, and Excelsior believes the same policy goal can be achieved by requiring robust equity participation. Nonetheless, Excelsior can and will comply with similar requirements that were contained in the August solicitation if the "no stripping" provision remains in the NOPR despite the inefficiencies and unnecessary costs it creates.

Finally, Excelsior is concerned about the provision in Section 609.10(d)(11) that appears to require that "all" intellectual property rights are to be available to DOE to "complete, operate, convey, and dispose of the defaulted project." While Excelsior has the utmost confidence that the Mesaba Energy Project will honor its debt obligations, DOE should have recourse only to the physical assets of a defaulting project for one simple reason: in the NOPR itself, DOE limits the loan guarantee so as not to cover any research, demonstration, and development (RD&D) costs that were incurred in the course of developing the project for which the Applicant is seeking a loan guarantee. Given that the Applicant has borne the RD&D burden, the intellectual property rights developed through that RD&D should remain with the Applicant, even in the unlikely event of a default.

Comments to Section 609.15

The provisions for process in event of default are generally acceptable, except for the great degree of uncertainty introduced by the last clause of Section 609.15(b). The vague discretionary authority DOE would confer upon the Secretary to determine whether the Loan Guarantee will be honored defeats the purpose of the Loan Guarantee Program itself. The uncertainty generated by a provision that provides the Secretary apparently unbridled discretion to deny a holder payment under the guarantee may pose an insurmountable bar to project development for projects, like IGCC, that must depend on government guarantees. Excelsior urges DOE to delete this provision.

Thank you for this opportunity to comment.

Sincerely,

Julie Jorgensen
Co-President and CEO, Excelsior Energy Inc.